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ABSTRACT

This essay examines the various economic effects of U.S. trade with developing nations to determine whether or not such trade is in the U.S. interest. Expansion of trade with the Third World is very much in keeping with the Reagan administration's economic goals. It stems from the conviction that solution to the problems of poverty and insufficient economic development is to be found in the magic of the market place. U.S. gains from trade include access to needed raw materials, consumer benefits, economic efficiency, and growing markets for U.S. exports. Although U.S. trade with the developing countries is quite favorable (with the exception of oil), it is not sufficient to look exclusively on the positive side. One serious cost to the United States is loss of employment opportunities in declining industries. Study after study identifies the same industries as being most sensitive to import competition: textiles and clothing, footwear, leather goods, and consumer electronics. Compared to a protectionist stance, the article concludes, in the long run, a set of policies to stimulate world trade and distribute its costs equitably carries with it a much greater potential for improving the economic well-being of all nations. (RM)

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US Trade with the
Third World:
The American
Stake

John A. Mathieson
Occasional
Paper 28

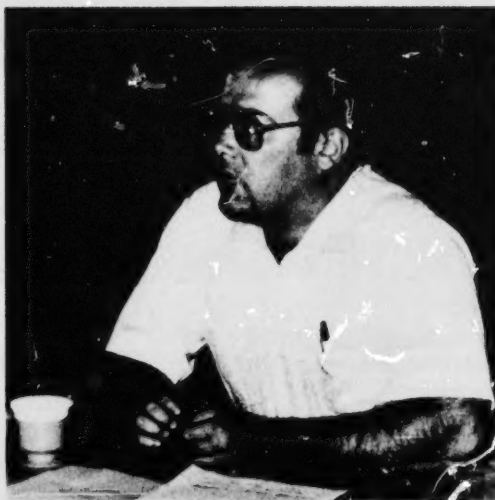
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About the Essay

Trade is the primary form of international economic transaction. A great majority of these commercial flows are managed by private business but take place within governmental regulations and institutions. Consequently, trade is closely related to official policies.

Expansion of trade with the Third World is very much in keeping with the Reagan administration's economic goals. John Mathieson points out that world interdependence must be recognized, particularly in times of economic stagnation. He notes related costs, citing job dislocation as a major problem which must be solved. And he reviews the benefits to be gained, evaluating the US stake as positive and growing. Compared to a protectionist stance, he concludes, "In the long run, a set of policies to stimulate world trade and distribute its costs equitably carries with it a much greater potential for improving the economic well-being of all nations."

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US Trade with the Third World: The American Stake

Introduction

In contrast to its predecessors, the Reagan administration has indicated as an explicit statement of policy that private sector transactions constitute the core of US relations with developing countries. The rationale for this policy is in part based on a tactical effort to blunt proposals for greater governmental programs, particularly foreign aid, to assist the developing countries. It also stems, however, from the genuine conviction that the solution to the problems of poverty and insufficient economic development is to be found, in the words of President Reagan, "... in the magic of the market place."

This new-found wisdom is in fact only confirming what has for some time been the reality of the relationship. While the emphasis given to the role of the private sector has certainly become more pronounced, private transactions, primarily international trade and investment, have for years far exceeded official monetary flows between the United States and developing countries. In 1980, for example, the total US foreign aid program amounted to some \$7 billion, a good part of which was extended for security reasons rather than development purposes. By comparison, the United States imported \$118 billion worth of goods from developing nations in 1980 and sold \$83 billion worth of products to those countries. The stock of foreign direct investment in developing countries by US firms totaled over \$52 billion at the end of 1980.

These figures alone are sufficient to underscore the importance of private enterprise in US-Third World relations and to dispel the widely held myth that developing countries are merely impoverished, often ungrateful recipients of US aid. One should not, however, write off foreign assistance as unnecessary since many developing nations, particularly the poorest countries of Sub-Saharan Africa and South Asia, have little opportunity to expand their export earnings and attract investment inflows. These countries will continue to require aid to maintain existing levels of production and consumption, much less to grow out of the misery of poverty.

Among all the various forms of international economic transactions, trade is paramount. The importance of comparative advantage and of the potential gains from trade was established hundreds of years ago. In fact, the roots of modern economic analysis, found in writings of Adam Smith and David Ricardo, were based on a discussion of the merits of trade. Despite a growing involvement of state-owned enterprises, the great majority of commercial flows are managed by private businesses. However, this commerce takes place within the context of rules, regulations, and institutions that are designed and operated by governments. As a result, official policies have a marked effect on the forms and levels of trade flows.

Given the importance of international trade to both developing countries and the United States and given the basic orientation of the current US administration, it is appropriate to take stock of the nature of trading relationships and policies that shape them. A prudent course of action on trade matters could enhance the growth performance of all nations involved and could provide the additional benefit of improving US-Third World relations.

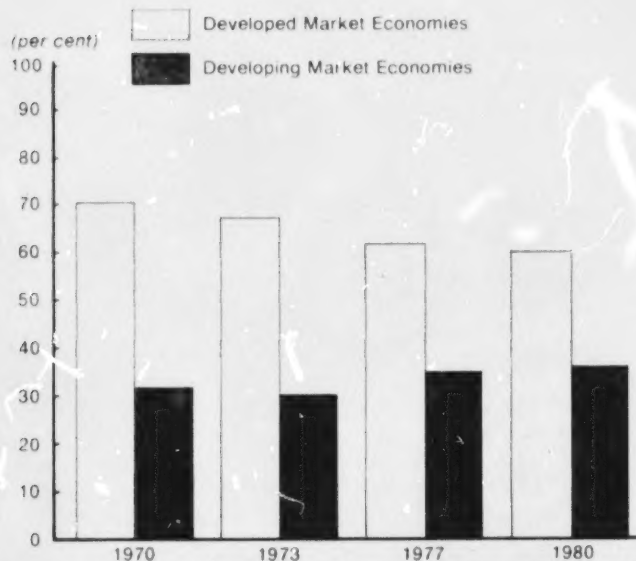
The Nature and Growth of US Trade with Developing Countries

Developing countries are playing a large, rapidly growing role in US trade relations to the point where developing country growth can directly affect US economic performance and well-being. However, misconceptions concerning the nature of US-developing country trade have led to faulty conclusions concerning the resulting costs and benefits. Analysis of the macroeconomic aspects of this trade reveals little of a surprising nature other than the pace of growth and the fact that, in spite of its many positive features, US-Third World trade has been subject to vehement debate and criticism.

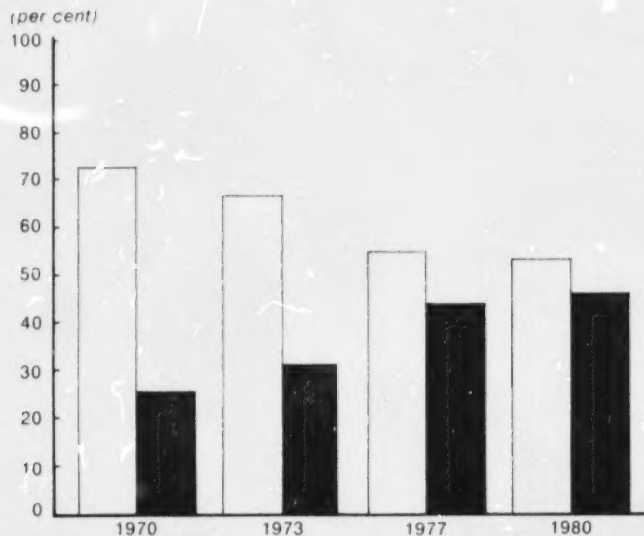
While the composition of US transactions with individual developing countries varies enormously, trade between the United States and the Third World as a whole follows a predictable pattern: machinery, transport equipment and other categories of capital goods, and sophisticated manufactures, along with agricultural products, dominate US exports to the developing countries. These countries in turn sell oil, raw materials, tropical foodstuffs, and labor-inten-

US Exports to and Imports from Developed and Developing Countries¹
as Share of Total U S Exports and Imports
(percentages)

EXPORTS



IMPORTS



sive consumer goods to the United States. Although there are some exceptions, this general pattern accounts for the bulk of US-Third World trade and follows closely what would be expected as a result of major differences in comparative advantage and resource endowment. That is, the United States has a relative abundance of land, capital (both physical and human), and technology, and the developing countries have a relative abundance of raw materials and unskilled and semiskilled labor.

Developing countries purchased 38 percent of total US exports of goods in 1980; 30 percent were bought by non-OPEC developing countries and 8 percent by members of OPEC. The developing countries purchased 31 percent of US primary commodity exports and 41 percent of US manufactured exports. US sales of manufactures to developing countries have risen dramatically, from \$8 billion in 1970 to \$62 billion in 1980, growing at an average annual rate of 23 percent. A significant part of this increase is accounted for by major increases in manufactures exports to members of OPEC, but manufactures exports to other developing countries also rose rapidly.

In previous decades, US exports to the industrialized countries grew at a faster rate than exports to developing countries. However, this trend was reversed in the 1970s when the average annual growth rate of US exports to the Third World was 21 percent, compared with an annual growth rate of 17 percent for US exports to industrialized countries. During the last decade, therefore, the OPEC and non-OPEC developing countries represented the most rapidly expanding markets for US exports. OPEC and non-OPEC developing country purchases from the United States grew at annual rates of 23 percent and 20 percent respectively.

The growing importance of developing countries to US trade is even more striking with respect to imports. The Third World as a whole was the source of some 26 percent of total US imports in 1970. By 1980 this share had risen to 48 percent, primarily because US purchases of greater volumes of higher priced fuel products had increased from \$2 billion in 1970 to \$67 billion in 1979. OPEC's share in total US imports rose from 5 percent to 22 percent over this period, whereas the non-OPEC developing countries' share rose as well, from 21 percent to 27 percent. From 1970 to 1980, US imports from non-OPEC developing countries grew at

U S Trade, 1980¹ **(\$ billions and percentages)**

U S Exports		U S Imports		U S Exports		U S Imports	
\$220.7 billion		\$240.8 billion		\$220.7 billion		\$240.8 billion	
Canada	16.0%		17.2%				
EEC	24.3%		14.9%	Manufactured Products	55.8%	48.3%	Manufactured Products
Japan	9.4%		12.7%				
Other Developed Market Economies	8.3%		5.7%			7.7%	Food, Beverages, and Tobacco
OPEC	8.0%		21.6%	Food, Beverages, and Tobacco	13.8%		4.6% Crude Materials ¹
							3.6% Chemicals ²
Non-OPEC Developing Market Economies	30.0%			Crude Materials ¹	11.7%		
			26.7%	Chemicals ²	9.4%		32.8% Mineral Fuels ³
				Mineral Fuels ¹		3.6%	
Centrally Planned Economies		3.5%	1.0%	Miscellaneous	5.7%		3.0% Miscellaneous

¹Includes (inter alia) raw hides and skins, crude rubber, logs and lumber, and oil and fats.

²Includes fertilizers.

³Includes lubricants and related materials.

NOTE: Export and import figures are f.a.s. (free alongside ship) transaction values. Totals include trade with unidentified countries not otherwise shown on this table.

an average annual rate of over 22 percent, compared to a less than 17 percent growth rate of US imports from industrialized countries. Particularly important in this respect is the growth of manufactured goods imports from non-OPEC developing countries, which grew at a rate of over 27 percent annually during the 1970s. The share of manufactures in total US imports from these countries increased from about one-third in 1970 to nearly one-half by the end of the decade.

US imports of manufactured goods from non-OPEC developing countries are highly concentrated in terms of both suppliers and commodities. Just five countries (Mexico, Taiwan, Hong Kong, South Korea, and Brazil) account for three-fourths of total US manufactured imports from non-OPEC developing countries. These imports are heavily concentrated in a relatively few categories of commodities. Consumer goods and manufactured products classified chiefly by material (textiles, metals, plywood, etc.) account for as much as 70 percent of all Third World exports of manufactures to the United States. Consumer goods (textiles and clothing, footwear, and consumer electronics) make up the lion's share (50 percent) of US imports of manufactures from the Third World. These are also the US industries considered "sensitive" to import competition since they employ large numbers of US workers and because their markets can be penetrated rapidly by imports.

In spite of the large volume of US exports to developing countries, the United States is experiencing a significant merchandise trade deficit *vis-à-vis* the Third World amounting to some \$36 billion in 1980. This has stimulated complaints of "exported jobs" by certain sectors in the United States. But the aggregate figure is deceiving. Of the total \$118 billion in US imports from developing countries in 1980, \$67 billion, or about 57 percent, was accounted for by gas, oil, and petroleum products. The United States continues to record large surpluses in manufactured goods trade with developing countries, a surplus of some \$29 billion in 1980.

Although merchandise trade does represent the strongest economic link between developing countries and the United States, overconcentration on the merchandise component of the balance of payments can be misleading. For example, US income from service exports (e.g., investment income, fees

and royalties, shipping and insurance, and interest income) has a positive effect on the US current account balance. The United States ran an overall services surplus of almost \$36 billion in 1980. Over \$23 billion of this surplus was accounted for by developing countries, including oil exporting countries. This surplus directly offsets a portion of the trade deficit in the current account balance.

The US Stake

Like any other set of commercial transactions, international trade carries with it economic costs and benefits. In order to determine whether or not on balance US trade with developing countries is in the US interest, it is necessary to sort out the various economic effects of this trade.

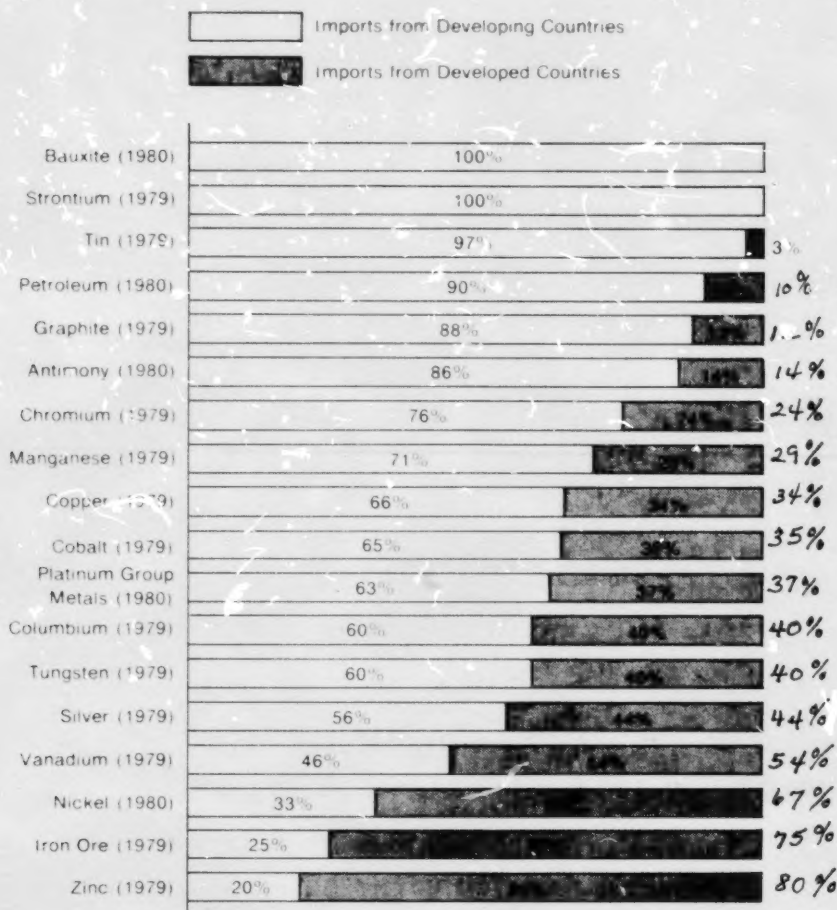
US Gains from Trade

Access to needed raw materials. By emphasizing the manufactured goods component of US trade and its employment impact, the trade debate often neglects the importance of minerals and other primary commodities imports. The importance of oil imports is evident. About one-half of total petroleum supplies available to the United States are imported; 90 percent of these imports come from developing countries. Although the United States produces large quantities of some nonpetroleum minerals, such as iron, lead, copper, and phosphates, it relies heavily on imports for others. For example, US imports from developing market economies account for 100 percent of domestic consumption of columbium and strontium. The Third World supplies more than one-half of the bauxite, tin, cobalt, and other materials vital to US industry. In the case of certain agricultural commodities, such as natural rubber, coffee, cocoa, hard fibers, and jute, imports from the Third World account for all US consumption. While the importance of individual Third World commodities to our economic activity and consumer welfare varies, these imports constitute a major element of US-developing country interdependence.

Consumer benefits. US imports of manufactures from developing countries generally fall into the category of consumer goods in the lower price ranges. Being of relatively low cost, goods such as clothing, shoes, appliances, and consumer electronics permit higher levels of consumption and/or the release of funds for the purchase of other goods and increasingly expensive services. It has been argued that imported

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US Imports of Selected Metals and Minerals¹ (percentages of total imports)



goods do not result in consumer savings, since retailers merely mark up prices on imports to make them equivalent to domestically produced goods. An analysis based on a survey of actual US retail sales tends to refute this assertion.⁴ This study found imported products from all areas to cost 10.8 percent less than comparable domestic goods. More importantly, while imports from developed countries (Europe, Japan, and Canada) were only marginally less expensive (0.4 percent), imports from developing countries (Latin America and Asia, excluding Japan) were as much as 16.3 percent less expensive than domestic products of the same quality.

These goods are purchased and consumed primarily by families with lower incomes and can make a contribution to moderating the impact of inflation. In the basket of products bought by low-income families, import prices were 13.1 percent less than domestic prices. As an indication of the impact of US imports from the developing countries on American prices, US consumer prices over the 1967-80 period rose by an average of 7.2 percent per year, whereas apparel prices increased only 4.2 percent annually, and prices for home electronics actually fell almost 1 percent per year.

Looking at it from a different perspective, another recent study estimated that the effects of protectionist measures imposed by the United States between 1975 and 1977 resulted in a cost to consumers of \$660 million in sugar, \$1,250 million in carbon steel, \$400 to \$800 million in meat, \$500 million in television sets, and \$1,200 in footwear.⁵ These and other studies consistently indicate that US consumers are major beneficiaries of trade, particularly trade with developing countries.

Efficiency gains. Imports from the Third World result in important indirect economic benefits to the US economy, most of which are related to economic efficiency. Increased trade with developing countries has the following benefits:

1. Larger markets encourage greater economies of scale.
2. Increased exports stimulate investment and encourage faster growth rates.
3. Import competition encourages cost-cutting technological change, which increases the overall efficiency of the economy.

4. Domestic price inflation is inhibited by greater competition from abroad, thus permitting more aggressive macroeconomic policies to reduce unemployment and stimulate growth.
5. Greater low-cost imports free domestic resources that were allocated inefficiently in industries in which the United States has little comparative advantage to move into more productive activity.⁶

Efficiency gains through international trade are dispersed widely throughout the economy and do not lend themselves to simple quantification. Therefore, efficiency as an objective often holds a lower priority than such measurable objectives as achieving full employment or balanced trade. However, efficiency is a fundamental prerequisite to the attainment of a healthy economy. To a large extent the current economic malaise in the United States results from lags in investment, research and development expenditures, and productivity. Efforts to make the United States a more efficient, competitive producer are far more likely to rekindle US growth than measures that have the effect of subsidizing inefficient industries. Increasing the fundamental efficiency of US industry should be the essence of any "supply side" economic strategy.

Growing markets for US exports. Due to its abundance of resources and the size of its domestic market, the US economy, when compared with most other countries, has historically been relatively isolated from international trade. This situation is rapidly changing. US exports as a percentage of gross national product have risen from 5 percent in 1960 to 13 percent in 1980. Exports are estimated to account for one of every eight jobs in the manufacturing sector and for the production of one-third of the farm acreage in the United States. Exports now exceed business fixed investment and are over three times the amount spent on residential construction, which are both important indicators of the health of the US economy.

As noted earlier, more US goods and services are purchased by developing countries than by many countries and areas that traditionally have been among the major markets for US exports. These exports not only benefit firms in the export sector but also provide many jobs. An estimated 500,000

Twenty Largest US Trading Partners, 1980⁷

(\$ billions and percentages)

The twenty largest U S trading partners, in terms of total merchandise transactions, include eleven developing countries, which together account for more than 25 per cent of all such transactions and 33 per cent of all U S imports. Mexico is the third largest trading partner of the United States.

	Total Transactions	Exports	Imports
Canada	\$ 76.9	\$ 35.4	\$ 41.5
Japan	51.5	20.8	30.7
<u>Mexico</u>	27.6	15.1	12.5
West Germany	22.7	11.0	11.7
United Kingdom	22.5	12.7	9.8
<u>Saudi Arabia</u>	18.3	5.8	12.5
France	12.7	7.5	5.2
<u>Nigeria</u>	12.1	1.2	10.9
<u>Taiwan</u>	11.1	4.3	6.8
Netherlands	10.6	8.7	1.9
<u>Venezuela</u>	9.9	4.6	5.3
Italy	9.8	5.5	4.3
Korea, Rep.	8.8	4.7	4.1
Belgium-Luxembourg	8.6	6.7	1.9
<u>Brazil</u>	8.0	4.3	3.7
<u>Libya</u>	7.6	0.5	7.1
<u>Hong Kong</u>	7.4	2.7	4.7
<u>Algeria</u>	7.1	0.5	6.6
<u>Indonesia</u>	6.7	1.5	5.2
Australia	6.6	4.1	2.5
Total, 20 Countries	\$46.5	\$157.6	\$188.9
Total U S Trade	\$461.5	\$220.7	\$240.8
11 Developing Countries as % of Total U S Trade	27.0%	20.5%	33.0%

NOTE: All figures are f.a.s. (free alongside ship) transaction values.

US citizens are employed in the production of manufactured products to be sold to the oil-importing developing countries alone. There is a great deal of potential for continued growth in US exports, since demand in the developing countries is far from satiated and could expand rapidly as these countries advance economically.

Costs to the United States: Economic Dislocation

Although US trade with the developing countries is quite favorable (with the exception of oil), it is not sufficient to look exclusively on the positive side. US imports of manufactured goods from the Third World have grown rapidly, and while not large in a macroeconomic sense, these imports are concentrated in "sensitive" commodity categories, i.e., those requiring labor-intensive production and those competing with stagnating or marginally competitive sectors in the US economy. This type of trade leads to the classic case of increased efficiency in the economy as a whole and welfare gains to consumers but losses of employment opportunities in declining industries. The welfare gains are significant, but they are dispersed widely throughout the economy, whereas displacement of employment opportunities is concentrated in relatively few industries. Study after study identifies the same industries as being most sensitive to import competition—textiles and clothing, footwear, leather goods, and consumer electronics.⁸ These are the very industries which figure prominently in petitions for trade adjustment assistance filed over the past few years.

Examinations of the actual or potential employment effects of trade with developing countries are complicated by numerous methodological problems, the lack of sufficient data, and preconceived notions concerning what conclusions should result. Those who favor liberalized trade tend to underrate and even ignore adverse effects that may occur. Likewise, advocates of protection tend to exaggerate the adverse effects of imports and to understate the gains.⁹ To summarize a growing body of literature on the subject, most but not all analyses conclude the following:

- The net impact of shifts in foreign trade on aggregate US employment has been very small in recent years.¹⁰
- Economic development in the United States and other industrial countries entails significant adjustment in economic structure, including a shift of employment away

from labor-intensive manufacturing and toward services and more sophisticated manufacturing industries. The growth of manufactures imports from developing countries is not the fundamental cause of this latter shift, which would occur in any event, but accelerates the shift.

- Despite the minor macroeconomic employment effects of growing imports from developing countries and the fact that export-related job opportunities are opened up from this trade, certain industries have suffered relatively large losses in employment and will continue to do so in the future.
- In response to major shifts in comparative advantage, trade restrictions would prove costly, ineffective, and far less preferable than positive adjustment policies.

For several reasons the problem of job displacement cannot be brushed away with broad statements about economic efficiency and structural change. First, the sectors involved are large and important to the US economy. Just four economic sectors—electric and electronic equipment, textile mill products, apparel and other textile products, and leather and leather products—accounted in mid-1981 for as much as 24 percent of total US employment in manufacturing. Second, these and related sectors are strongly represented by trade unions; since imports are subject to action by the federal government (whereas automation, shifts in demand, and many other factors affecting employment are usually not), unions have focused a great deal of attention on job displacements related to trade. Finally, a strong case can be made that the burden of employment dislocation falls heavily on disadvantaged, low-skilled laborers.

The problem of economic dislocation cannot be ignored. As a former labor union official put it, "(the labor movement) . . . is not willing to be sacrificed on the altar of economists' dogmas—even if the dogma be as hallowed as the theory of comparative advantage."¹¹ The employment disruptions caused by trade are politically sensitive because of their high visibility to affected unions. Where adjustment between sectors is difficult, a strong coherent program to deal with economic dislocation is needed to offer workers temporary income and health plan maintenance, assurance

of retirement benefits, retraining, and relocation. Structural adjustment programs must be seen as more than palliatives to restrain protectionist pressures.

The Two-Way Street of Trade

Unless developing countries can export to the United States and other industrialized countries, they will not be able to earn the foreign exchange that in turn allows them to purchase needed goods, services, and technology from the developed countries; repay their increasing debts; and grow.

Whether trade promotes growth or growth promotes trade is a question reminiscent of the chicken and egg controversy. Some believe that exports are an "overspill" of domestic output, once production becomes efficient by international standards. Others feel that exports are stimulated by world demand, thereby resulting in more rapid domestic growth. Regardless of theoretical causation, the link between growth and trade is clear in practice. Countries with relatively strong export performance also tend to have relatively high growth rates. The more foreign exchange a country can earn, the more it can buy from others those items it finds expensive or impossible to produce at home; and the faster it can get on with the job of making its economy more efficient. In addition, "Exports do not rely on charity, nor imply a heavy burden of repayment later, as do concessional loans. Therefore, exports are the highway to self-sufficiency, to earning one's way."¹²

The developing countries have benefited from the expansion of world trade since World War II, but even these gains have not been enough; gaps in trade, income, and well-being between developing and developed countries continue to grow. While the Third World accounted for three-fourths of the world population in 1979, its share of world exports accounted to only 28 percent. Manufactures accounted for only 22 percent of the total exports of developing market economies (including the OPEC countries) in 1979. In contrast, 75 percent of the exports of developed market economies were manufactured products, which tend to have more stable prices and to embody higher levels of domestic inputs than do primary commodity exports, thus contributing more to domestic income and employment.

These and other indicators demonstrate gaps of develop-

ment and well-being between rich and poor countries. Third World countries require greater levels of income and employment if they are to have any chance of meeting their own needs. While international trade is no panacea, increasing developing countries' access to world markets is a step in the right direction.

Trade Policies Toward Developing Countries

In recent years, an ambivalent attitude has emerged in the United States and other developed countries toward trade with the Third World. Historically, the concept of "nonreciprocity" has been applied to North-South trade; developing countries receive the advantages of tariff and non-tariff liberalizations by industrialized countries without being expected to offer equivalent reductions in their own trade barriers. In addition, industrialized countries have put into place Generalized Systems of Preference (GSPs) under which certain developing country exports are able to enter the markets of the industrialized countries duty free or with reduced duties. But these preferential systems are limited in scope. In the US system, for example, a number of "sensitive" items, primarily labor-intensive manufactures such as shoes and textiles, are not covered since preferential treatment is deemed harmful to domestic producers. Additional items can be removed from the eligible list under an escape clause. In addition, the "competitive need" clauses in the US system (i.e., imported commodities from individual countries achieving a 50 percent market share or an overall quantitative limit, about \$45.8 million per product in 1980) result in individual commodities being removed from eligibility.

Third World exports have expanded under these provisions. However, there has been a resurgence of protectionism since the mid-1970s in the United States and in other developed countries as a consequence of stagnant economic conditions and rising unemployment. The industrialized countries have erected numerous trade barriers, particularly against products of strong interest to the developing countries. These restrictions have generally taken the form of quantitative ceilings on exports and have euphemistically been called "voluntary export restraints" or "orderly marketing arrangements" (OMAs). Most countries have tightened existing quotas or imposed new ones to limit developing-country exports of textiles and clothing, governed by the Multifiber Arrangement. The United States

and other countries have at times imposed quotas or OMAs limiting developing-country exports of footwear and color television sets. A number of restrictive devices regarding steel imports have been introduced. These and other measures designed to "protect" domestic industries from foreign competition directly limit the export potential of developing countries, delay needed adjustments in developed countries, and represent an inflationary and costly means of income support to protected industries. It has been estimated that the consumer cost of greater protection in the apparel industry could be as high as \$81,000 per job.¹³

But despite these heavy costs of growing protectionism to the industrial countries, the political battle against protectionist pressures is often very difficult. It is difficult because the temporary losses from trade liberalization are visible and vocal, whereas those who gain are generally dispersed and disorganized. Thousands of housewives spread over the whole economy often have less voice than a textile worker with a job at stake. But in the long run what is really at stake is not just cheaper shoes, clothes, and bedspreads, but the jobs and living standards of the whole population.¹⁴

Effects of the Tokyo Round

The ambivalence of current policies toward developing countries is best illustrated by the outcome of the Tokyo Round of multilateral trade negotiations.¹⁵ In the Tokyo Round a key goal of the United States and other industrialized countries was to ensure that the developing countries start participating fully in the trading system organized under the General Agreement on Tariffs and Trade (GATT) in order to change GATT's image as a "rich man's club." The actual results of the Tokyo Round appear to be a mixed blessing for the developing countries, therefore Third World nations have not enthusiastically rushed to sign the agreements.

With respect to tariffs the agreement resulted in an average decline in duties worldwide of about one-third, with reductions being phased in over an eight- to ten-year period. However, the average duties on developing-country exports will decline by only about 25 percent. Moreover, a number of items of specific importance to the developing countries were not even subject to negotiation. Finally, several product categories, particularly textiles, are subject to restricted trade through non-tariff barriers, and so tariff reductions on those items will have little impact on trade.

Despite these limitations, the benefits of the Tokyo Round tariff cuts to the developing countries should not be viewed as insignificant. The Tokyo Round reductions are roughly comparable to those of the Kennedy Round, and the post-Kennedy Round experience showed that at least some developing countries were very successful in expanding their exports of manufactures. Some countries have also been successful in coping with quantitative restrictions either by diversifying product lines and markets or by upgrading the quality of goods exported within quantitative limits. Finally, several Third World countries already have (or soon will have) the capacity for competing in markets for sophisticated products which are subject only to low tariffs and few quotas.

Since industrialized country tariffs have already reached relatively low levels (e.g., duties levied on imports to the United States, which averaged 53 percent before World War II, have been reduced to about 7 percent), actions taken on non-tariff barriers to trade are a much more significant aspect of the Tokyo Round. These involved basic changes in the GATT framework and agreements on several codes of conduct on specific non-tariff barriers (NTBs).

To the developing countries, the most important changes in the GATT framework are 1) the inclusion of the so-called "enabling clause," which provides a stronger legal basis for nonreciprocity, allowing developed countries to extend differential and more favorable treatment to developing countries on a non-most-favored-nation basis, and 2) a developing-country commitment to assume fuller GATT obligations as their economies develop. This principle of "graduation" requires that special treatment be phased out as economic progress is made. The developing countries were particularly adamant about the first of these changes, and the industrialized countries conditioned their support of the enabling clause on developing-country commitment to the principle of graduation.

The NTBs addressed by the Tokyo Round package of agreements include the following:

1. Subsidies and countervailing duties.
2. Standards, that is, technical barriers to trade.
3. Government procurement.

4. Licensing.
5. Systems of customs valuation.

The concept of graduation is meant to apply to at least a number of the codes. Developing countries that do not sign the codes may or may not be granted the privileges embodied in the provisions. The United States and the European Economic Community (EEC) are taking the position that, in the case of some of the new codes, particularly those on subsidies and government procurement, they will only commit themselves to applying the benefits to signatories.

Safeguards and Curbs

Throughout the Tokyo Round the major dispute between developing and certain developed countries involved the proposal for a safeguards code. Article XIX of GATT, which permits countries to impose safeguards (temporary restrictions such as higher tariffs or import quotas designed to protect industries suddenly threatened by a large volume of imports), has not worked well in the past. Countries desiring to impose import restrictions have not wanted to be subject to its many provisions and, therefore, often have taken actions not covered by GATT rules. The proposed code broadened the definition of restrictive policies, included a clause requiring that imports be proven to cause serious injury to domestic producers, and strengthened mechanisms for consultation, surveillance, and dispute settlement.

By placing currently "informal" import curbs within the framework of GATT, this code is designed to regulate trade controls. It could, however, be used to justify a proliferation of restrictions aimed at developing countries. The safeguards dispute has resulted in a stalemate; the code has yet to be completed and signed by any country, although negotiations have continued. The developing countries are in a difficult position: implementation of the code as proposed could be used to their detriment, yet the absence of any agreement on safeguards leaves developed countries free to impose unilateral restrictions or to demand "voluntary" export restraints.

The outcome of the trade negotiations reflects the ambivalence prevailing in the international environment and the way in which developing countries are viewed by estab-

lished industrial powers. On the one hand, Third World countries are seen as vital new centers of commerce and growth. As such they deserve greater opportunities and a more important role in the system, on more equal terms with industrial countries. On the other hand, at least some developing countries are feared as supercompetitors capable of supplanting industrial production in the developed countries. As a result, the Tokyo Round Agreement represents a major effort to keep the trading system as open as possible, but at the same time it thrusts new responsibilities on certain developing countries and raises the possibilities for what some term "orderly trade" and others call "codified protectionism."

A New US Export Consciousness

In the United States, a great deal of attention has recently been focused on export performance and policy. Historically, due to the size and depth of the US market, only the largest US firms made much of an effort to expand overseas sales. US export policies, formulated over a period of continuous trade surpluses, tended to infuse other foreign policy objectives into commercial transactions. Rising trade deficits in the 1970s and 1980s have stimulated an active reassessment of export policies and procedures.

Current action in the export sector concentrates on two areas—removing disincentives to exports resulting from specific US policies and pressuring other countries to dismantle what are considered unfair incentives or subsidies to their own exports. Export groups are lobbying to eliminate or reduce the effect of such policies as the Foreign Corrupt Practices Act, antiboycott provisions, various embargoes, and certain antitrust provisions. While the US government has not taken strong actions to remove "disincentives" in many of these areas, it has vigorously pursued efforts to arrive at uniform export incentives on an international basis. The US emphasis on the subsidies code in the Tokyo Round is a case in point. The United States also applied major pressure on Brazil to dismantle its subsidies program. Recently the United States has sought to reach agreements with other major exporters on some standardization of interest rates for official export financing to avoid excesses in competitive bidding. In a similar vein, the US government and private sector have strongly urged those countries with large trade surpluses *vis-à-vis* the United States, developed and developing alike (such as Japan, Korea, and Taiwan), to step up their purchases of US products.

The "export consciousness" of the United States is beginning to develop, but it has not yet had much of an impact on policy. A more aggressive stance is clearly noticeable in the statements and actions of the Reagan administration officials. While this shift in attitude is long overdue, an export orientation should not be extended to the extremes of mercantilistic policies, which would inevitably prove counterproductive.

A Future of Inward-Looking or Outward-Looking Policies?

The industrialized countries seem to be incapable of regaining the relatively high rates of growth and low inflation and unemployment levels experienced in the 1960s and early 1970s. Factors underlying this economic sluggishness include:

1. Reductions in productivity growth.
2. Higher prices for natural resources and growing costs associated with environmental protection.
3. Less technological innovation and expenditures for research and development.
4. Sociological and demographic changes that are locking nations into more "secure" social patterns.

In reaction to these trends, the developed countries have placed a much higher priority on price stability than on growth, have become more resistant to economic change, and have attempted to insulate their domestic economies from international developments. In sum, these countries are looking inward for solutions to their economic problems. This economic "nationalism", while not as pronounced as that which played a large hand in creating the Great Depression of the 1930s, pervades the thinking of some policy makers and major interest groups. While based on legitimate concerns, this thinking tends to disregard the reality of world economic interdependence. An outward-looking strategy based on global efficiency holds much more promise than a "beggar-thy-neighbor" approach.

The essence of the global efficiency argument is that the greatest growth potential now lies in the developing countries, which could in fact become an "engine of growth" for

the world economy. Important indications of Third World potential include their relatively low capital/labor ratios, their abundance of labor and natural resources, and the opportunity for applying existing technology already utilized in the rich countries.

As the developing countries have grown and become more fully integrated into the international economic system, their impact on the economic performance of the United States and other industrialized countries has grown considerably and will continue to grow. The developing countries represent increasingly significant markets for industrial-country exports. Higher demand in the Third World—however generated—helps to stimulate the developed countries in ways that are certainly no more and maybe even less inflationary than equivalent domestic expansion efforts. During the 1974-75 recession, the fact that developing countries maintained high levels of imports from the industrial countries had a perceptible impact in modifying the adverse impact of economic downturn in the industrial countries.

In order to sustain their levels of demand in an era of high energy and food prices, the developing countries have had to borrow heavily from the international capital and credit market. The cumulative debt of the developing countries rose to as much as \$450 billion by the end of 1980. While the Third World nations will have to adjust their economies to seek greater balance in their international payments, their only hope for servicing this debt will be to earn foreign exchange through exportation.

A strategy of North-South economic cooperation holds promise for establishing a basis for renewed world growth, similar to that founded on the Bretton Woods system 35 years ago. As a development strategy, however, it is designed to achieve long-run mutual gains, and so near-term problems associated with trade must be addressed.

The Need for Dynamic Economic Change

In spite of all the benefits associated with US trade with developing countries, no adequate solution to the major cost borne by this trade—job dislocation—has yet been found. In fact, sectoral dislocations and general unemployment represent a domestic economic problem much more fundamental than import competition from developing and developed countries.

Trade policies are not appropriate instruments to achieve full employment. The proper policy instruments for dealing with general unemployment are monetary and fiscal policies to create sufficient and noninflationary aggregate demand. The best method to defuse protectionist pressures is to establish domestic growth. But current conditions strongly suggest that traditional measures are not enough and that there is a need for an effective US labor market policy and a US development strategy.

The plain fact is that real trade adjustment can only take place in a healthy, adaptable economy. The experience of the last two decades suggests that such an economy will be possible only when the United States commits itself to a policy of national economic development, based upon a careful appraisal of needs, resources, and opportunities.¹⁶

The complexity and difficulty of implementing positive adjustment policies should not be underestimated. Numerous adjustment plans have been applied in the United States and elsewhere, involving dislocations from trade and other factors such as technological innovation and military base closings; the results have been mixed. The US strategy for adjusting to economic dislocations has been haphazard and piecemeal. Many thought the past US trade adjustment assistance programs were poorly managed and failed to address issues of major importance to those being required to adjust.¹⁷ Many "adjustment" programs have the effect of freezing existing patterns of production and resisting change rather than affecting genuine structural improvement by shifting workers into industries and regions where they could both produce more and earn more.

The development of an effective adjustment program requires changes in attitudes and policies on a broad range of economic issues such as: national planning, trade policies, business incentives and disincentives, labor market interventions, maintenance of income, retirement benefits, and health insurance coverage. Changes in these areas would not only encounter major bureaucratic constraints but more importantly would confront deep-seated differences in economic and social ideologies. The magnitude of these problems should not, however, be used as an excuse for avoiding necessary actions.

The Reagan administration has adopted strong fiscal and monetary measures designed to revitalize the US economy. Regardless of the relative merits of this approach, it is important that the domestic program be complemented by an international component. Domestic efficiency can be enhanced only within the context of international interdependence. Trade can act as a driving force to improve national efficiency and productivity.

This argument is consistent with the basic philosophy of US officials in the administration, but its implications do not call for a "hands off" policy on the part of the government. Official actions are required in several areas.

First, as the largest economy in the world, the United States must take the lead in pressing for a more liberal trading environment and forestalling the natural tendency, particularly in times of recession, to revert to protectionist measures. Developments in the next several years are likely to shape the world's trading environment for the remainder of the century. The Tokyo Round trade agreements are largely complete, but they have yet to be fully implemented and authority remains for continued negotiations to make the pacts more acceptable to all participants. In the fall of 1982, a ministerial meeting of GATT members will be held to assess what progress has been made on implementing the Tokyo Round agreements and to initiate the negotiation of outstanding concerns. This meeting represents an important opportunity to take the interests of developing countries fully into account and to find appropriate means to involve the Third World nations more comprehensively in the GATT framework.

Second, the United States, along with other industrial nations, surplus oil countries, and oil-importing developing countries, must take on the task of finding solutions to the increasingly urgent problem of Third World debt. The debtor nations will have to bear a major share of the adjustment burden. So long as they are subject to growing current account deficits and crushing levels of debt, there is little likelihood that the international economy as a whole can reestablish past levels of economic expansion and stability.

Finally, while the United States has a positive and growing stake in trade with developing and developed countries, this nation will have to become more adaptive to increasing

international interdependence. Specifically, a policy is needed to deal humanely with the problem of job dislocation (from trade or other causes) and at the same time to effect more efficient shifts of labor and capital resources from declining to expanding industries. Generating growth at the macroeconomic level is a necessary but insufficient solution. No nation has found a fully satisfactory answer to the adjustment problem but that does not mean that such a solution does not exist.

Looking at the entire range of US policies toward the Third World, the Reagan administration is currently at odds with developing countries on many issues, such as foreign aid, the Law of the Sea Negotiations, and efforts to undertake "global negotiations" to reform the world economy. Trade, however, is one crucial area where the philosophy of the administration and the interests of developing countries coincide. US initiatives to move toward a more open world trading environment could, therefore, result in a marked improvement in US-Third World relations.

Looking toward the future, it is difficult to determine whether major trading nations, including the United States, will undertake inward-looking or outward-looking policies. A "selective" protectionist stance, permitting orderly growth in trade but also condoning ad hoc restraints on trade in particular sectors, may appear attractive in the short run, but eventually the adverse effects of inward-looking policies and reduced trade would be recycled to the United States and other countries in the form of greater inflation, more unemployment, and slower growth. In the long run, a set of policies to stimulate world trade and distribute its costs equitably carries with it a much greater potential for improving the economic well-being of all nations.

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